Death in Service/Life Insurance Trust

The choice of those over the Inheritance Tax threshold who also have large death in service, insurance policies and pension funds.

Inheritance Tax (IHT) remains an 'avoidable tax' and nowhere is this truer than in the field of Death in Service Benefits, Life Insurance and Pension Funds.

Death in Service benefits are not subject to Inheritance Tax (IHT) when they arise on the death of the employee, but there is a trap. They become taxable on the death of the recipient (usually the surviving spouse) and should they result in the total estate exceeding IHT Nil Rate Band threshold (currently £325,000), up to 40% of their value may be lost.

Insurance Policy proceeds are IHT exemption death if they go to the widow, or if they are written in trust, but the same trap applies. If the widow's estate is pushed over two Nil Rate Bands by the payout (he or she can normally claim the benefit of a second NRB) by the payout, up to 40% may again be lost.

The answer to this problem is to set up a trust in your lifetime, with the express purpose of receiving Death in Service benefits or Life Insurance. The cash is then kept out of the widow's estate for tax purposes and the possibility of ever paying 40% tax on it is overcome.

Every I0 years, funds in the trust over the Nil Rate Band prevailing at that time will be subject to a small IHT charge (up to 6%) but even this can be avoided (or at least minimised) by the setting up of ***multiple*** Life Insurance Trust where the sums concerned are large.

The problem of the harsh Income Tax treatment of income from the trust (currently 50%) can also be overcome by converting it (once running) into a 'Life Interest' trust which enjoys a much gentler tax regime.

All in all, these Trust's are highly recommended for all whose death benefits and life insurances would lift the family's wealth over £650,000 (2 current Nil Rate IHT Tax bands).